



Financial Sector Deepening

*Reaching out to the
low end of the market*

Liza Valenzuela
USAID
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Outline

- Intro - The case for deepening
- First and second generation reforms
- Country reforms exercise
- Success stories: Peru and Bolivia
- Common pitfalls

Introduction

- Financial liberalization is good...
- But, it doesn't automatically lead to financial sector deepening

A broad array of financial services supplied by a diverse set of actors and made available to and demanded by the low end of the market.



The Case for Deepening

- LAC: 70% of EAP depends on micro and small enterprises (MSEs)
- Represent some 60 million (consumer) households
- GDP produced by MSE's reaches 40% in Brazil, Mexico, Dominican Republic
- Only some 3% of these firms have access to adequate financial services

IMPLICATIONS ????

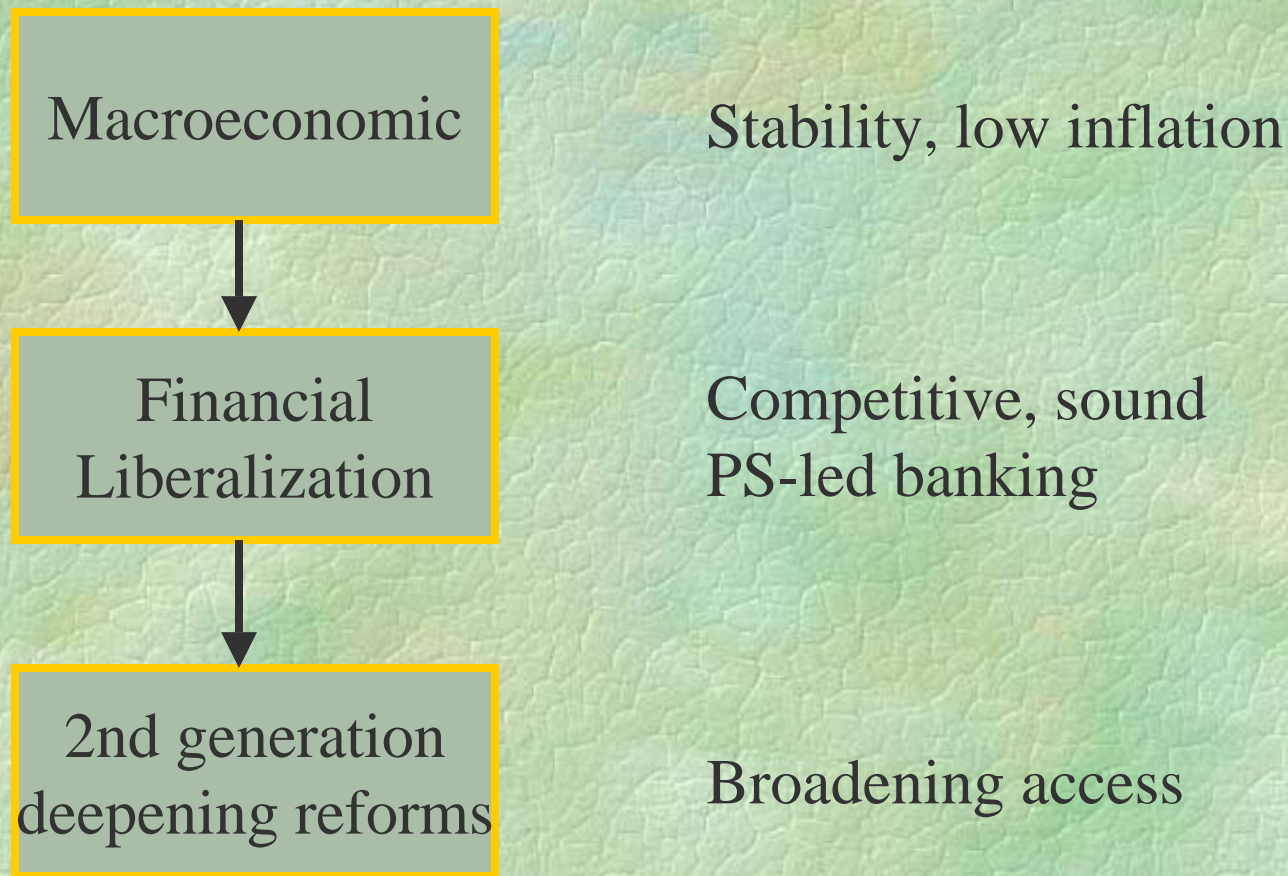
Indicators of Depth

- Most common
 - M2/GDP
 - credit to private sector/GDP

- New emerging indicators
 - number of deposit accounts, urban/rural
 - number of small loans from banks & others



Sequencing of Reforms



1st generation

Financial Liberalization Reforms

- Freeing interest rates
- No more subsidized, directed credit
- Free barriers to bank entry (incl. foreign)
- Regulation and supervision
- Independence of supervisor
- Privatize state banks (or assured firewalls)

2nd generation

Deepening Reforms

- Improved Regulation & Supervision
 - Entry of new actors (NBFIs)
 - Ease operating restrictions
 - branch hours, branch location, mobile banks, regional or national coverage, ownership
 - Appropriate Supervision
 - loan documentation, collateral, provisioning, reporting requirements
 - Legal Reserves/other ratios -- sensible levels

2nd generation

Deepening Reforms

(Cont.)

- Legal/institutional framework
 - movable assets law, leasing
 - taxation of NGOs
 - functioning and speedy court process/ ADR
- Market infrastructure/Public Goods
 - credit bureaus, rating services, transparency
- Strengthening of alternative institutions

Financial Sector Institutions

- Banking
- Non-Bank Institutions
 - Insurance (life and general)
 - Mutual funds
 - Contractual savings (housing, pension)
 - Securities market (inc. brokers/dealers)
 - Alternative finance



Alternative Institutions

- Credit Unions
- Finance companies/consumer lenders
- Equity building societies
- Leasing
- NGOs
- others (including more informal)
- State banks (exception to the rule)

Exercise

A look at four countries...

*What is hindering or promoting
financial sector deepening?*

TASK

1. Which country has most depth?
2. What policies hinder and which facilitate depth?

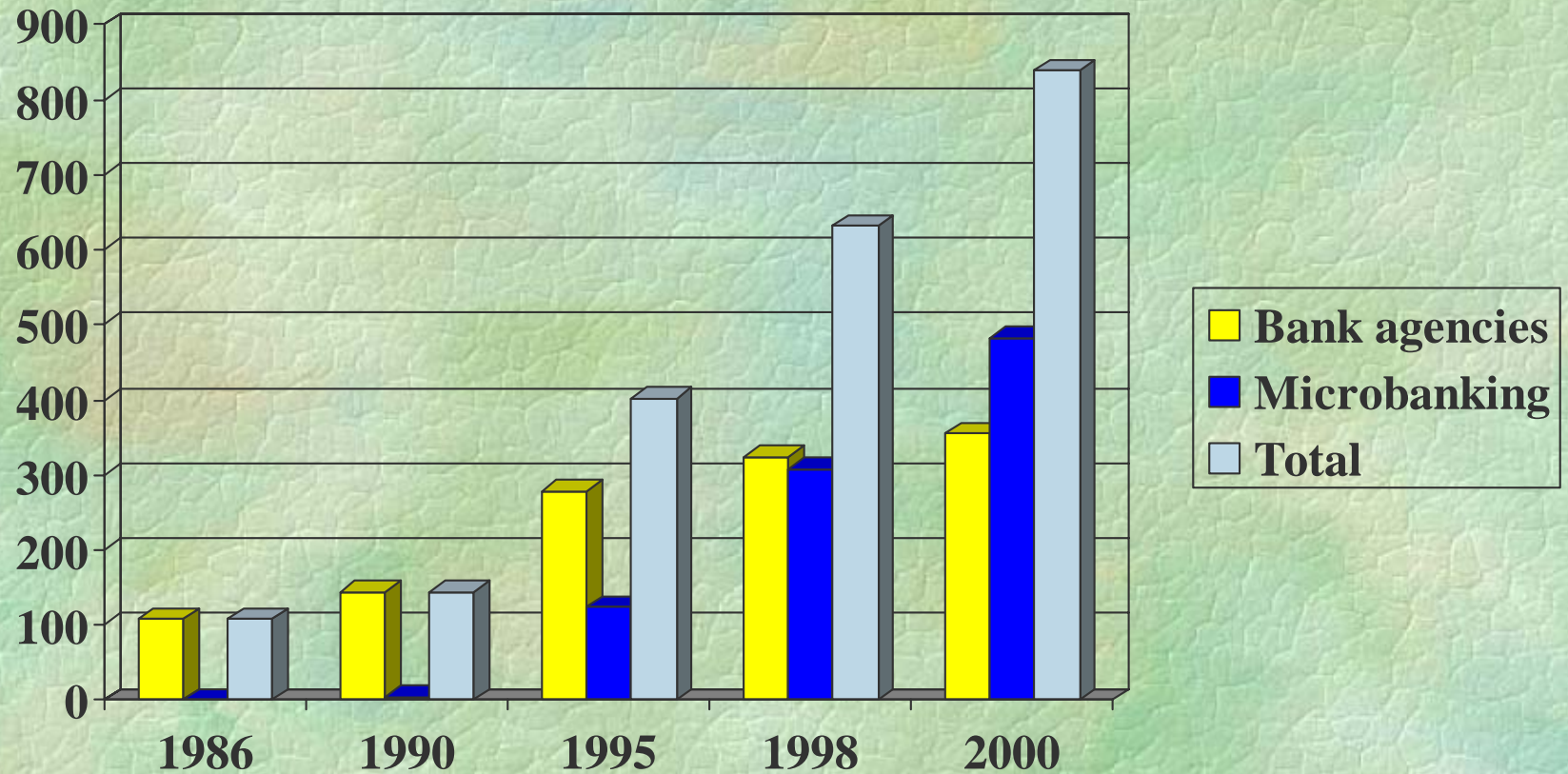


Financial Deepening: Bolivia

		1992	2001	change
Portfolio	Portfolio banks	2.4 billion	3.3 billion	36%
	Portfolio microbanking	200 million	775 million	291%
Borrowers	Borrowers banks	102,000	179,000	75%
	Borrowers microbanking	93,000	451,000	370%
Deposits	Deposits banks	1.2 billion	2.9 billion	139%
	Deposits microbanking	194 million	811 million	318%
Accounts	No. savings accounts banks	236,000	658,000	179%
	No. savings accts microbanking	224,000	797,000	259%

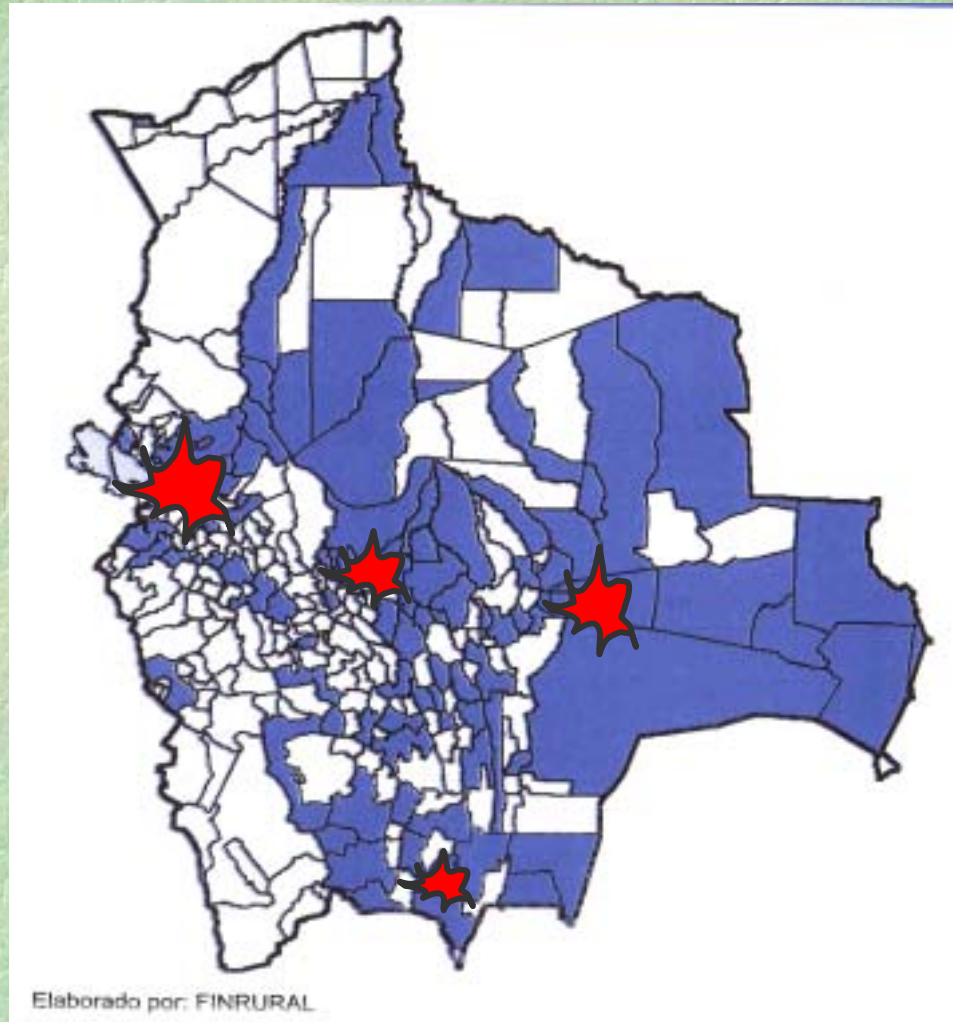
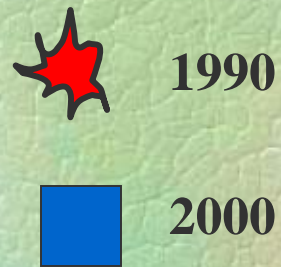
*Population 8.3 million*¹³

Bolivia: Evolution of Agency Coverage 1986-2000



Source: Finrural, 2000

Bolivia 2000: Coverage of Financial Services



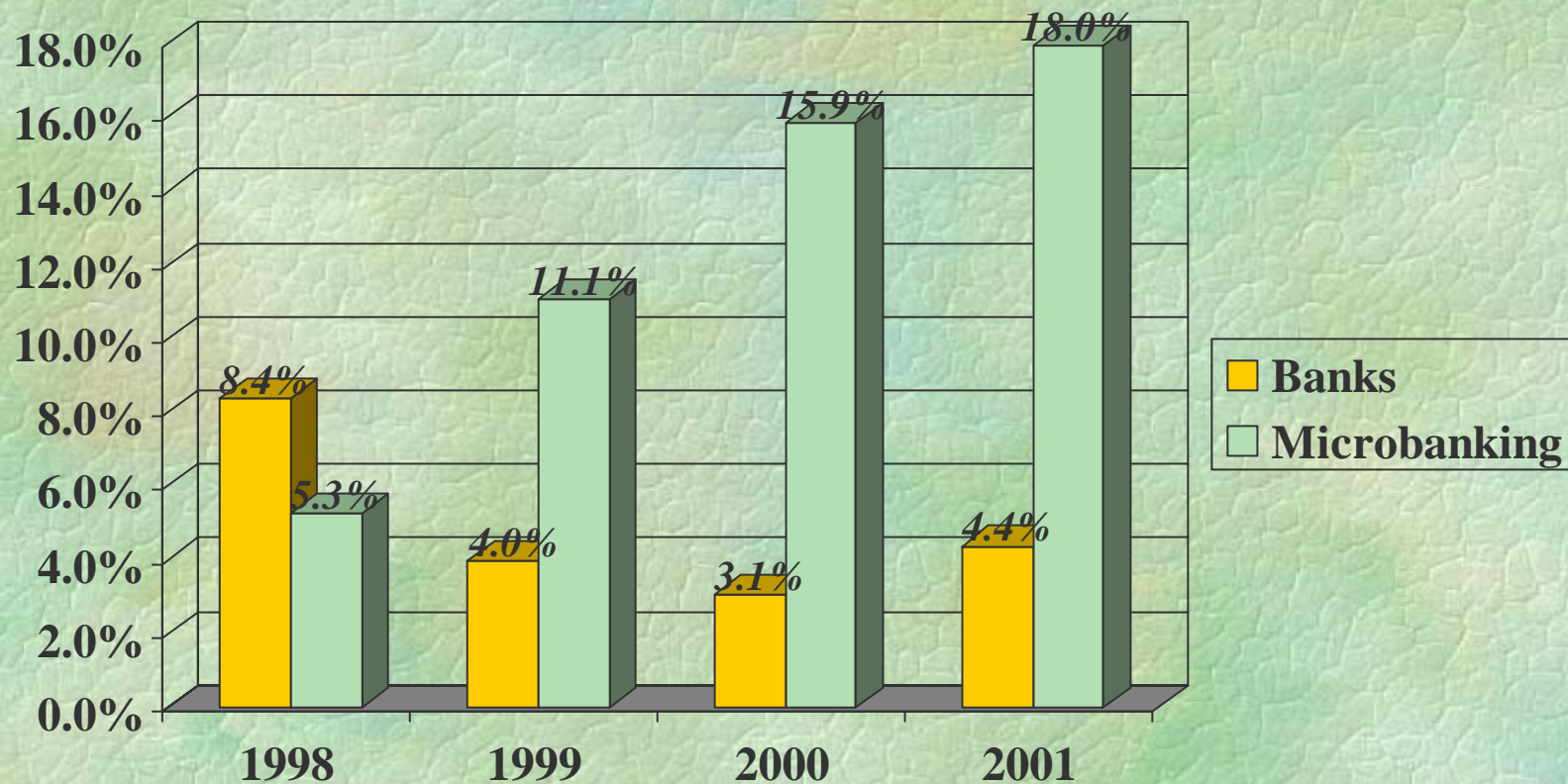


Financial Deepening: Peru

		1992	2001	change
Portfolio	Portfolio banks	2.0 billion	10.7 billion	426%
	Portfolio microbanking	101 million	1.0 billion	907%
Borrowers	Borrowers banks	331,952	1,397,308	321%
	Borrowers microbanking	206,001	1,171,079	468%
Deposits	Deposits banks	3.6 billion	13.1 billion	260%
	Deposits microbanking	59.5 million	455 million	666%
Accounts	No. savings accounts banks	4,120,000	5,096,893	24%
	No. savings accts microbanking	149,000	783,260	424%

*Population 25 million*¹⁶

Peruvian Commercial Banking Sector & MFI Profitability 1998-2001 (ROE)



Source: MicroRate and Superintendancy Reports



Five Common Pitfalls

- Financial liberalization incomplete
- Entry -- too lax or too stringent
- Regulations too prescriptive
- Specializing microfinance/crowd out
- Inadequate/inappropriate supervision